KAISER RESOURCES LTD.

1972 ANNUAL REPORT

KAISER RESOURCES LTD.

Box 2000
Sparwood, B.C.

1401 Board of Trade Tower
1177 West Hastings Street
Vancouver, B.C.

Westshore Terminals Ltd.
Roberts Bank
Delta, B.C.

AUDITORS
TOUCHE ROSS & CO.
Vancouver

TRANSFER AGENT
CANADA PERMANENT TRUST CO.
Vancouver, Calgary, Winnipeg, Toronto, Montreal

REGISTRAR
NATIONAL TRUST COMPANY LIMITED
Vancouver, Calgary, Winnipeg, Toronto, Montreal

SHARES LISTED
Vancouver, Toronto, and Montreal Stock Exchanges

ANNUAL GENERAL MEETING
FERNIE HIGH SCHOOL, FERNIE, B.C., JUNE 19, 1973.

1972 AT A GLANCE

		Year Ended December 31		
		1972	1971	1970**
Shipments (Long tons)		**4,289,000**	4,014,000	2,274,000
Sales		**$81,657,000**	68,934,000	10,274,000
Other Revenue		**$ 1,222,000**	1,365,000	101,000
Costs & Expenses		***$95,899,000**	85,647,000	15,074,000
Net Loss	*Before Extraordinary Charge*	**$ 5,657,000**	—	—
	After Extraordinary Charge	***$13,020,000**	15,348,000	4,699,000
Loss Per Share	*Before Extraordinary Charge*	**.56**	—	—
	After Extraordinary Charge	**$ 1.30**	1.53	.47
Depreciation & Depletion		**$12,582,000**	10,559,000	835,000
Capital Expenditures		**$ 6,660,000**	21,987,000	18,834,000
Long-term Debt		**$83,650,000**	99,811,000	77,277,000
Shareholders' Equity		**$36,955,000**	49,975,000	65,323,000
Average Number of Employees		**1,517**	1,497	1,389

*Includes extraordinary charge of $7,363,000.

**Certain figures are not directly comparable with succeeding years because of operations start-up provisions in 1970.

DIRECTORS

*EDGAR F. KAISER, Chairman

*GRAHAM R. DAWSON, Vice-Chairman

*STEPHEN A. GIRARD, Chairman, Executive Committee

JACK J. CARLSON, President and Chief Executive Officer, Kaiser Steel Corporation

PAUL G. DESMARAIS, Chairman and Chief Executive Officer, Power Corporation of Canada Limited, Montreal

*ROGER T. HAGER, Chairman, The Canadian Fishing Company Limited, Vancouver

EDGAR F. KAISER, Jr., Executive Vice-President Operations, Kaiser Resources Ltd.

ROLAND A. KJELLAND, Executive Vice-President Finance and Administration, Kaiser Resources Ltd.

W. B. MacDONALD, Former President, A. E. Ames & Co., Toronto

IAN N. McKINNON, Chairman and President, Consolidated Natural Gas Limited, Calgary

*E. E. TREFETHEN, Jr., President, Kaiser Industries Corporation

E. D. H. WILKINSON, Q.C., Partner, Russell & DuMoulin, Barristers and Solicitors, Vancouver

*Member, Executive Committee

IN MEMORIAM

Directors were saddened by the death of their colleague, J. Leonard Walker, who passed away on February 3, 1973, in Montreal. A prominent Canadian businessman, Mr. Walker had served on the Board of Kaiser Resources for three years.

Edgar F. Kaiser was elected Chairman of the Board to succeed Jack Ashby, who retired. Stephen A. Girard, President and Chief Executive Officer, was appointed a Director and Chairman of the Executive Committee. Also appointed to the Board were Edgar F. Kaiser Jr., Executive Vice-President, Operations, and R. A. Kjelland, Executive Vice-President, Finance and Administration. Other Directors who retired from the Board were C. F. Borden, C. Lee Emerson, R. G. Heers, C. A. MacIlvaine and William Marks.

OFFICERS

EDGAR F. KAISER, Chairman of the Board

GRAHAM R. DAWSON, Vice-Chairman of the Board

STEPHEN A. GIRARD, Chairman of the Executive Committee, President and Chief Executive Officer

EDGAR F. KAISER, JR., Executive Vice-President, Operations

ROLAND A. KJELLAND, Executive Vice-President, Finance and Administration, and Treasurer

ROBERT W. MacPHAIL, Vice-President and General Manager

B. E. OLSEN, Vice-President, Sales

W. P. POPENOE, Vice-President, Administration Controller, and Assistant Secretary

HOWARD E. CADINHA, Vice-President, Corporate Planning

JOHN W. FEIST, Acting Secretary

WILLIAM S. BARNUM, Assistant Secretary and Assistant Treasurer

TO OUR SHAREHOLDERS

During 1972, interim price increases negotiated with Japanese coal customers and the results of management's program for improving coal production enabled Kaiser Resources to reduce its operating loss. The Company's loss from operations was $5,657,000, or $.56 per share, on sales of $81,657,000. These results compare with a net loss of $15,348,000 or $1.53 per share, on sales of $68,934,000 in 1971. A 1972 extraordinary loss of $7,363,000, or $.74 per share, resulting from writedowns in values of certain plant and equipment, increased the year's net loss to $13,020,000, or $1.30 per share.

Since last year's Report, the Company's capital and other programs for overcoming major operating difficulties have achieved these improvements:

. . . The modified Elkview coal preparation plant is producing finished coal at tonnage rates and quality specifications meeting the current interim agreement with Japanese customers.

. . . Modifications to the 25-yard shovels and the 200-ton trucks, together with revisions in the ongoing preventive maintenance program, are increasing the availability of mining equipment.

. . . Training programs and housing assistance for employees at the mine and the coal processing facilities are helping to achieve gains in productivity and to reduce the employee turnover rates.

. . . As a safeguard against interruptions of rail service on the 700-mile haul between the mine and the port, the Company has built up its stockpiles of coking coal at its Westshore Terminals port facilities. At January 31, 1973, there were 409,000 long tons stockpiled at the port, enough coking coal to meet normal shipping schedules for about four weeks.

Looking to the immediate future, significant further improvement in the Company's operating results cannot be anticipated for the first half of 1973. Beyond June 30 of this year, Kaiser Resources' prospects depend on the outcome of current negotiations relative to its long-term coal sales contract and its financial restructuring, including a program for additional capital investment. (For further details relating to the sales contract and the Company's financial position, please see the Financial Summary and Notes to the Financial Statements included in this Report.)

In Japan, negotiations with our Japanese customers are continuing with respect to revisions in the sales contract. At the same time, we are intensively pursuing all the many facets to the Company's financial restructuring. These financial discussions include a possible equity position by the Japanese; potential additional investment by Kaiser Steel Corporation; rescheduling of the Company's long-term debt commitments; and obtaining the consents required from Kaiser Resources' and Kaiser Steel's lending institutions in order to finalize a refinancing program. With respect to the discussions about a possible equity program, we have asked our financial advisors to give consideration to the Company's Canadian and other public shareholders for the purpose of offering them an opportunity to participate on a fair and reasonable basis.

Results of these vital negotiations on contract revisions and refinancing will be announced promptly as definitive conclusions are reached. Every effort is being exerted to conclude these intensive discussions by June 30, 1973. Meanwhile, it would be inappropriate and premature to speculate on the results.

We are convinced that our Japanese customers are confident of the Company's coal production capabilities and that they are looking to Kaiser Resources as a long-term source for coking coal. The support of our shareholders, the confidence and assistance of our customers and our suppliers, and the performance of our 1,500 employees have been essential factors in enabling management to make progress toward solving the Company's difficulties.

Sincerely,

Edgar F. Kaiser, Chairman

S. A. Girard, President
and Chief Executive Officer

April 16, 1973.

OPERATING REVIEW

MINE OPERATIONS

At the Sparwood operations in the East Kootenay region of British Columbia, the ongoing program to overcome major operational problems has resulted in the achievement of stabilized production tonnage and specifications. Current contract commitments are now being met. Revised mining plans based upon production at an annual rate of approximately 4.6 million long tons of coal have been implemented.

At the Elkview coal preparation plant, modifications started in 1971 were completed. This included installation of a new 5,000-horsepower dryer fan motor, which enabled the plant to meet contract moisture specifications. The $10 million modification program has converted the plant from a wet-and-dry processing facility to an all-wet facility and has increased the capacity of the plant to approximately 5.5 million long tons at 9.5 percent ash specifications with 0.5 percent tolerance.

At the underground operations, a total of 896,000 long tons of coal was produced during the year compared with 793,000 long tons in 1971. Of this, approximately 586,000 long tons were produced at the hydraulic mine, which utilizes a proprietary technique of Mitsui Mining Company and Kaiser Resources using high-pressure water to extract coal deposits. In 1971, hydraulic mine production was 542,000 long tons.

At the surface mining operations, further modifications were made to shovel and truck equipment. This program has been a continuation of equipment modifications begun in 1971. Modifications involved the shovel booms and sticks on the 25-yard shovels and corrections to the truck braking systems and frames on the 200-ton trucks. Further performance testing is proceeding to determine whether additional modifications may be necessary to the shovel booms and sticks in order to assure full performance.

Larger tires were installed on part of the fleet of 200-ton trucks and complete conversion to the new tires is expected to be completed this year. This program is expected to improve operating availability and reduce overall tire costs.

A revised preventive maintenance program for truck and shovel equipment was introduced in 1972. This program is expected to contribute to long-term improvement in equipment availability.

A decision was made in late 1972 to offer the 54 cubic yard dragline for sale because its performance in mountainous terrain did not meet original expectations. The dragline will be replaced by a more flexible truck and shovel operation.

WESTSHORE TERMINALS LTD.

At Westshore Terminals Ltd., the Company's bulk-loading port facilities at Roberts Bank south of Vancouver, 4,085,000 long tons of Kaiser Resources' coal and 766,000 long tons of coal and petroleum coke from other companies were loaded aboard ships for export markets. The volume from other producers in 1972 was less than had been originally anticipated. In 1971, a total of 3,814,000 long tons of Kaiser Resources' coal was shipped by Westshore Terminals.

Early in 1973, Westshore Terminals reached agreement with the International Longshoremen and Warehousemen's Union for a new two-year labor contract which extends to January 31, 1975.

In view of the Company's experience in January and February of 1972 with severe winter storm conditions which affected train transport of coal to Roberts Bank by CP Rail, Kaiser Resources undertook to build up its inventory at the port.

At January 31, 1973, the stockpile of Kaiser Resources' coal at Roberts Bank was 409,000 long tons, which was sufficient to meet anticipated shipping schedules for a total of approximately one month should there be interruptions to rail service from the mine to Roberts Bank.

Negotiations are currently being conducted with CP Rail to combine two separate contracts covering rail delivery of coal from Elkview. The contracts now cover 5-million long tons annually to 1974 and 3-million longs tons annually to 1985.

ENVIRONMENTAL PROGRAMS

Approximately $1 million was spent in 1972 to construct facilities to dispose of refuse from the coal preparation plant. The Company estimates that additional capital expenditures of $5 million will be required by 1976 under this program.

Further research and development work was carried out by the staff of the Company's Reclamation Department at Sparwood. This has included experimentation with growing trees, grasses and clovers on a total of 283 acres, composed largely of old pits, refuse dumps and fine coal refuse lagoons. The Reclamation Department also completed a three-year land reclamation plan for the years 1973 through 1975 which has been submitted for Government approval.

To control coal dust from CP Rail trains between Sparwood and Roberts Bank, a binding agent in water is being sprayed over loaded cars at Sparwood as weather conditions require.

A water spray system has also been installed at Roberts Bank to wash down empty cars leaving the port terminal. The Company is currently discussing with CP Rail further possible improvements in controlling dust from rail trains.

COMMUNITY DEVELOPMENT

During the year the Company completed construction of a residential housing subdivision in Fernie, issued additional second mortgages under its employee home ownership program and took over a group of duplex units in Sparwood as additional properties for rental to employees. By year-end home ownership assistance had been extended to 347 employees and their families and a total of 236 rental units were under Company management. A shopping centre was completed at Sparwood and now provides a variety of commercial facilities for the community.

FINANCIAL SUMMARY

SALES

Sales revenue in 1972 amounted to $81,657,000 on coal and coke shipments of 4,289,000 long tons. Of this total, 4,045,000 long tons were metallurgical coking coal shipped under contract to Japanese steel mill customers. All other shipments amounted to 103,000 long tons of coal and 141,000 long tons of coke and related products. In 1971, 4,014,000 long tons of coal and coke were shipped of which 3,634,000 long tons were metallurgical coking coal. All other 1971 shipments amounted to 246,000 long tons of coal and 134,000 long tons of coke and related products.

OPERATING RESULTS

Operations resulted in a loss of $5,657,000 or $.56 per common share excluding an extraordinary charge of $7,363,000 or $.74 per share attributable to writedowns of $4,734,000 related to the Company's 54-cubic-yard dragline and $2,629,000 to certain equipment and facilities no longer in use at the modified Elkview coal preparation plant. The total loss for 1972 was $13,020,000 or $1.30 per common share. In 1971, operations resulted in a net loss of $15,348,000 or $1.53 per common share. The 1972 results reflect favorable year-end adjustments of $2,269,000 related principally to revaluation of inventories and to revisions in certain cost provisions applicable to operations throughout 1972. Of these adjustments, $1,495,000 is applicable to the first nine months of 1972.

SALES CONTRACTS

During 1972 interim contract price adjustments were in effect on all metallurgical coking coal shipments made to our Japanese customers. The interim agreements in effect until June 30, 1972 provided for a price increase of $2.80 per long ton and special cost assistance of US $2.07 per long ton for an approximate total price of $19.18 per long ton. This price also applied to 380,000 long tons carried over from the second quarter and shipped in the month of July. Under this pricing arrangement U.S. $8,750,483 of special cost assistance was received of which U.S. $4,506,674 was recorded as revenue in 1971 and U.S. $4,243,809 in 1972. The Company has agreed to adjust the price of coal delivered after June 30, 1973 in such a manner that Mitsubishi would be compensated for all costs incurred by Mitsubishi in respect of the special cost assistance, including costs attributed to fluctuations in the Yen-U.S. dollar exchange rate. Significant adverse fluctuations in the exchange rate have occurred since that pricing arrangement came into effect.

The price in effect from July 1, 1972 to June 30, 1973 provides for a contract base price of $16.88 and an interim price increase of $1.85 bringing the aggregate price per long ton to $18.73. There is no obligation to compensate Mitsubishi in respect of any payments under the current interim price agreement. Efforts are being made to reach agreement on contract revisions modifying the price applicable after June 30, 1973.

If no agreement can be reached, the base contract quantities of 5,000,000 long tons per year, plus or minus 10 per cent at the buyer's option, at a base price of $16.88 per long ton with ash specifications of 8.75 percent with 0.5 percent tolerance, would apply until March 31, 1975 (the contract price reopener date). At that time either party can seek a price adjustment and in the event mutual agreement is not reached with respect to repricing, the contract would terminate one year after the respective reopening date (see Note 1 of the Financial Statements).

INSURANCE SETTLEMENT

In 1972 a settlement was reached with the Company's insurers for a business interruption insurance claim submitted as a result of a fire in December, 1971 in the preparation plant dryer facilities. Of the total final settlement amount of $1,509,000 (a reduction of $109,000 from the anticipated settlement amount reported in the third quarter) $534,000 was included in 1972 earnings, $813,000 was recorded in December, 1971 and $162,000 constituted deductible amounts and reimbursements for costs incurred to reduce claimable losses.

CAPITAL PROGRAMS

Capital expenditures for facilities and equipment totalled $6.7 million in 1972. These expenditures involved the purchase of additional auxiliary mining equipment, one 200-tone truck and one 100-ton truck, dryer modifications, normal replacement and improvement expenditures and approximately $1 million for refuse disposal facilities. Of the above amount, approximately $500,000 was expended by the Company's port subsidiary, Westshore Terminals Ltd. to complete a facility program begun in 1971 to accommodate coal movements from Fording Coal Limited to Japanese customers. At December 31, 1972, investment in plant, property and equipment at cost totalled $148.2 million, including $14.5 million for Westshore Terminals.

Current estimates indicate that capital expenditure commitments for 1973 will aggregate approximately $9,000,000 which includes a more flexible truck and shovel operation having an initial capital cost of approximately $2,000,000 to replace the dragline.

LONG-TERM DEBT

At December 31, 1972, consolidated long-term debt totalled $109.4 million including $25.7 million of installments due at various times in 1973. During the year payments were made to the Canadian banks in the amount of $1.4 million reducing the outstanding amount under the $35 million bank credit to $29.4 million. The full amounts are outstanding under the Canadian Bank $15 million credit agreement and the Japanese advances of U.S. $35 million. A total of $14.5 million was outstanding under a Westshore Terminals Ltd. financing agreement with two U.S. banks.

In June, maturities of approximately $11.1 million of long-term debt which otherwise would have become due during the twelve months beginning June 30, 1972 were extended until June 30, 1973. In connection with this extension, Kaiser Steel Corporation and Kaiser Industries Corporation have agreed jointly and severally to purchase $10.6 million of these amounts to the extent they are unpaid at June 30, 1973.

In December, 1972, the Company reached agreement with its Canadian banks whereby a $5 million line of credit was made available to June 30, 1973. At December 31 this credit was fully utilized. By March 31, 1973, the amount utilized had been reduced to $4 million. This credit is secured by inventories and receivables other than receivables due under the Company's long-term contract with Mitsubishi.

Also in December, the effective date of certain working capital requirements provided for in the bank credit agreements were postponed from December 31, 1972 to July 1, 1973. These provisions require that current assets must equal not less than two times current liabilities as defined in those agreements with working capital as defined of at least $10 million. At December 31, working capital as defined was approximately $797,000.

Under the terms of Kaiser Steel's bond indenture and the terms of its current bank credit agreement, until Kaiser Resources' debt guaranteed by Kaiser Steel is repaid ($96.8 million at December 31, 1972), Kaiser Steel is prohibited, without consent from its lenders, from making further investments in, advances to, or guarantees on behalf of Kaiser Resources. Kaiser Steel may make unsubordinated advances to Kaiser Resources of up to $5 million which must be repaid within 90 days (subject to consent of Kaiser Resources' Canadian banks), and cannot be reloaned until 30 days after payment. At March 31, 1973, none of these funds were borrowed by Kaiser Resources.

KAISER RESOURCES LTD.
and Subsidiaries

FINANCIAL STATEMENTS

CONSOLIDATED STATEMENT OF LOSS AND DEFICIT
FOR THE YEAR ENDED DECEMBER 31, 1972

	1972	1971
Sales	**$81,657,329**	$68,934,005
Other Revenue	**1,222,369**	1,364,990
	82,879,698	70,298,995
Costs and expenses:		
Cost of products sold	**58,318,328**	58,188,686
Selling, administrative and general	**7,474,441**	7,260,488
Interest on long-term debt	**8,622,496**	7,872,337
Depreciation and depletion	**12,581,869**	10,559,233
Amortization of preproduction and development costs	**1,539,832**	1,766,519
	88,536,966	85,647,263
Loss before extraordinary items	**5,657,268**	15,348,268
Extraordinary items — Note 11	**7,362,523**	—
Loss for the year	**13,019,791**	15,348,268
Deficit at beginning of year	**20,024,753**	4,676,485
Deficit at end of year	**$33,044,544**	$20,024,753
Loss per share of common stock		
Loss before extraordinary items	**$ .56**	$1.53
Extraordinary items	**.74**	—
Loss for the year	**$1.30**	$1.53

CONSOLIDATED STATEMENT OF SOURCE AND APPLICATION OF FUNDS
FOR THE YEAR ENDED DECEMBER 31, 1972

	1972	1971
Source of funds:		
Operations		
Loss before extraordinary items	$ 5,657,268	$15,348,268
Items not requiring an outlay of funds		
Amortization of preproduction and development costs and other deferred charges	1,588,041	1,941,980
Depreciation and depletion	12,581,869	10,559,233
	14,169,910	12,501,213
Funds provided by (used in) operations for the year	8,512,642	(2,847,055)
Long-term debt	2,373,068	34,318,762
	10,885,710	31,471,707
Application of funds:		
Purchase of property, plant and equipment and other assets — net	6,237,977	23,217,201
Reduction in long-term debt		
Repayment	4,004,141	7,573,684
Reclassification to current liabilities	14,530,113	4,211,589
	24,772,231	35,002,474
Decrease in working capital	13,886,521	3,530,767
Working capital deficiency at beginning of year	7,199,782	3,669,015
Working capital deficiency at end of year	$21,086,303	$ 7,199,782
Elements of working capital changed as follows — increase (decrease):		
Current assets:		
Cash	$ 404,464	$ 1,291,759
Trade accounts receivable	705,111	(1,300,102)
Insurance claims receivable	(258,329)	969,327
Inventories	4,227,108	(2,168,025)
Prepaid expense	59,023	50,678
	5,137,377	(1,156,363)
Current liabilities:		
Accounts payable	413,870	3,658,567
Employment costs and amounts withheld from employees	209,192	(721,195)
Accrued interest payable — parent company	—	(588,693)
Other accrued liabilities	(116,847)	(511,494)
Short term bank loans	(5,000,000)	—
Instalments due within one year on long-term debt	(14,530,113)	(4,211,589)
	(19,023,898)	(2,374,404)
(Decrease) in working capital	($13,886,521)	($ 3,530,767)

CONSOLIDATED BALANCE SHEET
AS AT DECEMBER 31, 1972

ASSETS

	1972	1971
Current:		
Cash	$ 2,769,818	$ 2,365,354
Trade accounts receivable	1,708,116	1,003,005
Insurance claims receivable	710,998	969,327
Inventories — Note 3	13,194,541	8,967,433
Prepaid expenses	209,759	150,736
	18,593,232	13,455,855
Other assets	2,923,108	3,345,531
Property, plant and equipment — at cost:		
Land	17,178,271	17,108,271
Buildings and land improvements	45,984,993	42,971,107
Machinery and equipment	84,899,410	82,261,371
Construction work in process	108,834	2,129,903
	148,171,508	144,470,652
Less: Accumulated depreciation and depletion — Note 4	29,475,006	12,490,158
	118,696,502	131,980,494
Deferred preproduction and development costs less amounts amortized — Note 4	19,398,661	20,905,633
Other deferred charges	673,249	754,318
	$160,284,752	$170,441,831

On behalf of the Board:

S. A. Girard, Director

R. A. Kjelland, Director

CONSOLIDATED BALANCE SHEET
AS AT DECEMBER 31, 1972

LIABILITIES

	1972	1971
Current:		
Accounts payable	**$3,986,495**	$ 4,400,365
Employment costs and amounts withheld from employees	**1,996,982**	2,206,174
Accrued interest payable — parent company	**1,263,355**	1,263,355
Other accrued liabilities	**1,715,557**	1,598,710
Short term bank loans	**5,000,000**	—
Instalments due within one year on long-term debt	**25,717,146**	11,187,033
	39,679,535	20,655,637
Long-term debt — Note 5	**83,649,761**	99,810,947

SHAREHOLDERS' EQUITY

	1972	1971
Capital stock — Notes 7 and 8:		
Authorized		
15,000,000 common shares of par value $1 each		
Issued and fully paid		
10,000,000 shares	**10,000,000**	10,000,000
Contributed surplus	**60,000,000**	60,000,000
Deficit	**(33,044,544)**	(20,024,753)
	36,955,456	49,975,247
Commitments and contingencies — Note 9		
	$160,284,752	$170,441,831

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

AS AT DECEMBER 31, 1972

Note 1 — General

In 1968, Kaiser Resources entered into contracts with Mitsubishi Corporation ("MSK") for the sale to Japanese customers of approximately 75,000,000 long tons of coking coal meeting certain specifications at the rate of approximately 5,000,000 long tons annually for 15 years commencing in 1970. These contracts provide for price reopenings at the end of the fifth (March 31, 1975) and tenth contract years, and for cancellation one year after the respective reopening dates in the event mutual agreement is not reached with respect to repricing at those times.

Unforeseen problems in the initial years resulting principally from the inability to achieve contemplated low stripping ratios and the inability to produce metallurgical coking coal meeting the sales contract specifications, resulted in the failure to meet quantity and specification requirements and necessitated substantial revisions in the original plan of operations.

During 1971 revised plans including the accelerated acquisition of certain mining equipment were developed and implemented, and certain modifications to the processing plant were completed. In addition, the company obtained during 1971 under amendatory agreements with MSK, an interim price increase of $2.80 per long ton, an amended annual delivery rate of coal, less stringent ash specifications and a special price increase in the form of a special cost assistance of U.S. $2.07 per long ton for the period June 11, 1971, through June 30, 1972. These prices also applied to 380,000 long tons carried over from the second quarter of 1972 and shipped during July.

The foregoing amendatory agreements anticipated that negotiations for permanent price adjustments would take place toward the end of the period ending June 30, 1972; and, with respect to the above special price increase, Kaiser Resources agreed to adjust the price for coal delivered after June 30, 1972 (changed to June 30, 1973 by the below referenced letter agreement of July 7, 1972), in such manner that MSK would be compensated for all costs incurred by MSK relative thereto, including fluctuations in the exchange rate between the Yen and the U.S. dollar. The company has received and included in revenue a total of U.S. $8,750,483 as payment of the special price increase of which U.S. $4,243,809 was received and included in revenue during 1972.

The Company was unable to conclude negotiations for a permanent price increase during 1972 and in the absence of such an agreement entered into a letter agreement dated July 7, 1972 effective July 1, 1972 providing for (a) a "Base Price" of $16.88 per long ton (b) an interim price increase of $1.85 per long ton on coal sold and delivered during the period July 1, 1972 to June 30, 1973 (c) ash specification of 9.50% during the same period and (d) a total quantity of 4,500,000 long tons during the same period.

The company has had continuing discussions with the Japanese relative to the establishment of a satisfactory permanent price agreement. As well, extensive discussions have taken place relative to an equity programme of additional capital investment by Kaiser Steel Corporation, capital investment by the Japanese and the re-scheduling of its long-term financing commitments.

Further discussions and meetings are scheduled to be held with the Japanese commencing in the latter part of the first quarter of 1973 with every effort being exerted by both parties to conclude such negotiations by June 30, 1973.

Under the present pricing provisions of the coking coal contracts as amended in 1971 and 1972 and as presently financed the company will continue to incur substantial

losses and will be unable to meet its financing commitments in either 1973 or subsequent years.

While no firm assurance can be given at this time, the company believes that the on-going negotiations with the Japanese during 1973 will provide a solution to its financial problems within its capabilities as supported by its parent, Kaiser Steel Corporation.

In addition to any performance as guarantor with respect to the loans set forth in Note 5, Kaiser Steel Corporation without any required consents from financial institutions may make additional unsubordinated advances of up to $5,000,00 for periods up to 90 days. The consent of Kaiser Resources Ltd. bankers would be required for any such unsubordinated advances by Kaiser Steel Corporation.

Note 2 — Basis of Consolidation and Accounting Presentation

The accompanying statements consolidate the accounts of the company and its wholly-owned subsidiaries, Balmer Mine Limited, Westshore Terminals Ltd., Kootenay Coal Contractors Ltd., and Mountain Veiw Realty Limited.

Current assets and current liabilities where applicable, have been translated from U.S. dollars at the rate of exchange prevailing at December 31, 1972. All other amounts have been translated at rates of exchange at the date of each transaction.

Note 3 — Inventories

Inventories are summarized as follows:

	1972	1971
Clean coal and coke at the lower of cost and market	**$ 6,634,942**	$ 1,180,772
Raw coal at the lower of cost and market	**305,201**	2,943,249
Operating supplies at average cost	**6,254,398**	4,843,412
	$13,194,541	$ 8,967,433

Note 4 — Amortization, Depreciation and Depletion

Deferred preproduction and development costs are amortized on a straight line basis over a 15 year period being the term of the original sales contract.

Depreciation of plant and equipment is on a straight line basis over the estimated useful life of the assets or 15 years whichever is the lesser.

Depletion is taken at a rate of 10c per ton of raw coal mined.

Note 5 — Long-term Debt

	Amounts outstanding at December 31, 1972 Classified as	
	Current	Long-term
(a) Term loans under Bank Credit Agreements	$13,550,000	$30,850,000
(b) Kaiser Steel Corporation	—	10,000,000
(c) Mitsubishi Canada Limited	8,333,300	26,945,450
(d) Bank of America National Trust and Savings Association and the United California Bank	2,414,446	12,072,231
(e) Crows Nest Industries Limited	309,421	—
(f) The Royal Trust Company	41,739	2,212,213
(g) Other long-term obligations	1,068,240	1,569,867
	$25,717,146	$83,649,761

(a) Bank credit agreements provide for term loans aggregating $50,000,000, repayable as to $35,000,000 in 25 equal quarterly instalments of $1,400,000 beginning June 30, 1971 and repayable as to $15,000,000 in 12 equal quarterly instalments of $1,250,000 beginning June 30, 1973.

The quarterly payments due from June 30, 1972 to March 31, 1973 totalling $5,600,000 have been deferred until June 30, 1973. Kaiser Steel Corporation and Kaiser Industries

Corporation have agreed to purchase these deferred amounts to the extent they are unpaid at June 30, 1973.

As at December 31, 1972 $7,350,000 of the loans is repayable in equivalent U.S. dollars. However, the company may at its option convert the U.S. dollar loans to Canadian funds.

Interest is payable at 1½% in excess of the Canadian prime commercial rate with a minimum rate of 8½% as to $37,050,000 of loan principal and at 1% in excess of Eurodollar inter-bank rate as to $7,350,000 of loan principal.

Kaiser Steel Corporation is guarantor of the loans.

(b) Repayment is subordinated to the extent of $5,000,000 under the $15,000,000 Bank credit agreement with subsequent payments applying equally to the reduction of the Kaiser Steel Corporation loan and the balance of $10,000,000 under the Bank credit agreement. Interest is payable at the prime commercial rate of the Bank of Montreal.

(c) Mitsubishi Canada Limited has advanced U.S. $35,000,000. Of this amount $25,000,000 is repayable at a rate of $1.00 per long ton of coal delivered commencing July 1, 1972 with minimum quarterly repayments of $1,250,000 thereafter plus a $500,000 repayment on June 30, 1972. The repayments due June 30, 1972 to June 30, 1973 totalling $5,500,000 have been deferred until June 30, 1973. Kaiser Steel Corporation and Kaiser Industries Corporation have agreed to purchase $5,000,000 of the deferred minimum quarterly repayments to the extent they are unpaid at June 30, 1973. The remaining $10,000,000 is repayable at a rate of 50c per long ton of coal delivered commencing January 1, 1974 with minimum quarterly repayments of $625,000 thereafter plus a $250,000 repayment on December 31, 1973.

Interest is payable quarterly at 3% in excess of the prime U.S. bank rate.

Kaiser Steel Corporation is guarantor of the loan.

(d) An obligation of Westshore Terminals Ltd. repayable in equal quarterly instalments of $575,000 U.S. beginning March 31, 1973, with interest payable quarterly at ½ of 1% in excess of the prime U.S. bank rate on 90 day loans.

Kaiser Steel Corporation is guarantor of the loan.

(e) Payable at $309,421 semi-annually February 1st and August 1st to and including February 1, 1973.

(f) Mortgages of Mountain View Realty Limited repayable in equal monthly instalments of $22,649 including interest at 10% to 11%.

(g) Payable in U.S. dollars at varying interest rates based on prime U.S. bank rate and Euro-dollar inter-bank rates.

Kaiser Steel Corporation is guarantor of these loans.

Note 6 — Deferred Income Taxes

The company has included in its 1972 Financial Statements depreciation of fixed assets and amortization of preproduction and development costs of approximately $12,000,000 which have not been claimed as an expense for tax purposes and will be available to claim against future taxable income.

The future income tax deduction resulting therefrom will approximate $6,000,000 and the accumulated future income tax deduction as at December 31, 1972 amounts to $11,400,000. Pending a determination of the matters outlined in Note 1, the company has chosen not to recognize this potential future tax reduction in the financial statements.

Note 7 — Capital Stock

As at December 31, 1972 Kaiser Steel Corporation holds 75% of the total issued common shares.

Note 8 — Restrictions on Payment of Dividends

The declaration and payment of dividends is presently prohibited under the terms of various long-term debt agreements.

Note 9 — Commitments and Contingencies

(a) The company has entered into a service contract with Mitsubishi Canada Limited for the period from December 9, 1970 to the end of the Japanese Sales contracts. The remuneration is payable in the amount of 10c per long ton of coal shipped pursuant to the Sales contracts.

(b) The company is committed to a production payment of 50c per ton to Crows Nest Industries Limited beginning January 1, 1977 to a maximum of $34,000,000.

(c) Effective February 1, 1971 an interim agreement was entered into committing the company to a royalty of $.15 U.S. per long ton of coal processed using the hydraulic mining technique. Upon termination of this agreement it is contemplated that the underground hydraulic coal mining operation will be conducted as a joint venture whereby the company will maintain a 70% interest.

(d) The company, through its wholly-owned subsidiary Westshore Terminals Ltd., has entered into a lease with the National Harbours Board terminating March 31, 1985 with two 15 year renewal options for the lease of land at Roberts Bank. The annual payments are approximately $285,000.

(e) The Bank credit agreements provide that the company must maintain net current assets equal to not less than two times current liabilities with net current assets of at least $10,000,000. The effective date of this covenant has recently been extended to July 1, 1973.

Note 10 — Remuneration of Directors and Officers

During 1972 eight directors received compensation as directors of $61,683 (1971; $47,750) and eleven directors who are officers of the corporation or its parent company served without compensation. Eleven officers, three of whom are directors, received a total compensation as officers of $407,135 (1971; $247,292), and eight officers who were also officers of the parent company served without compensation.

Note 11 — Extraordinary Items

Extraordinary items consist of a provision for the estimated loss on sale and abandonment of certain equipment and facilities.

AUDITORS' REPORT

To The Shareholders,
Kaiser Resources Ltd.

We have examined the consolidated balance sheet of Kaiser Resources Ltd. and its subsidiaries as at December 31, 1972, and the consolidated statements of loss and deficit and source and application of funds for the year then ended. Our examination included a general review of the accounting procedures and such tests of accounting records and other supporting evidence as we considered necessary in the circumstances.

As set forth in Note 1, the company will continue to incur substantial losses under the coking coal contracts as amended and will be unable to meet its financing commitments in either 1973 or subsequent years.

In our opinion, subject to the satisfactory resolution of the matters referred to in Note 1, these consolidated financial statements present fairly the financial position of the companies as at December 31, 1972, and the results of their operations and the source and application of their funds for the year then ended, in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Vancouver, B.C.
January 16, 1973.

TOUCHE ROSS & CO.
Chartered Accountants.

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RESOURCES

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